A Study on the Obstacle Factors for the Entry of Korean Companies into Latin American Markets and their Countermeasures

Chong-Suk Park*

Abstract

In the past, trades with the Latin American markets were not active since the South Korean companies simply considered them substitute markets whenever exports were slow. However, the importance of these markets is highlighted anew thanks to the signing of the Korea-Chile Free Trade Agreement (FTA). Presently, Latin American nations are pursuing FTA with various nations in the world, regardless of the geographic boundaries, in order to vitalize their economy and attract foreign capital. Despite these efforts to liberalize the market, Latin American regions continue to restrict importation by leveraging diverse set of trade regulation policies. This research examines trade regulation policies in the Latin American regions and proposes Korea's countermeasures.

Key Words : Latin American, trade regulation, FTA, and foreign capital

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I. Introduction

As the FTA between Korea and Chile was signed in 2004, Korea found a means to enter into the Latin American markets. Until this point, Latin American markets were not the target of attention due to an unstable regional economy and certain geographic characteristics. Recently, however, they are pursuing economic stability and growth through market liberalization and increased efforts to attract investment. The Korean perspective, characterized by structural problems including unbalanced exports that focus on limited product assortments as well as limited export markets, pioneering into new markets such as the Latin American regions is urgently called for.

Although signing the FTA with Chile may be perceived as laying the foundation for expanding export and paving the road for the Korean companies to enter these markets, the reality is that the Latin American regions are rather neglected markets when it comes to Korea's external relations. Until now, studies conducted on these regions were limited mostly to economic approach methods. Pamela Starr claimed in an article that the Latin American economy that suffered from the so-called lost decade of 1980's due to chronic hyperinflation could recover market stability with successful market reform.1) Another article concerning this written by Nicola Phillips analyzed changes and growth of Latin American regions following vitalization of regionalism such as the launch of the MERCOSUR.2) A third article by Nam-Kwon Mun analyzes economic effect after the signing of the FTA between Korea and Chile, targeting products that are traded between the two nations.3)

Presently, Korea can be said to have laid down the stronghold for entering into the Latin American markets through the FTA with Chile. However, researches on the Latin American regions' trade regulation policies are considered lacking. This research examines the current trade situation between Korea and Latin American regions, while analyzing market entry barriers following all types of trade regulation policies, and confirming counter measures are pursued.

II. Current Situation on the Trade between Korea and Latin America

1. Current situation on the trade by region

The current trade situation between Korea and Latin America analyzes nations that take up significant portion within the Latin American regions and the nations that trade with Korea significantly. Mexico, a NAFTA member-nation, is Korea's 9th export nation. As of 2007, exports increased 19.1% to 748 Billion USD compared to the previous year. Brazil, another nation that is emerging fast in Korea's export market, is manifesting a continual export growth rate, which is the result of the Brazilian government's market liberalization policy.

Meanwhile, Chile, the top IT nation in the Latin American regions, trade with Korea is increasing due to the Korea-Chile FTA. However, this trade is not profitable due to the rapid increase in the price of raw materials. In Argentina, export slowed down after the declaration of default in 2002. However, in 2003 the economy recovered and now export has been increasing every year.

<table>
<thead>
<tr>
<th></th>
<th>2003 amount</th>
<th>growth rate</th>
<th>2004 amount</th>
<th>growth rate</th>
<th>2005 amount</th>
<th>growth rate</th>
<th>2006 amount</th>
<th>growth rate</th>
<th>2007 amount</th>
<th>growth rate</th>
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</thead>
<tbody>
<tr>
<td>Mexico</td>
<td>2,455</td>
<td>1.0%</td>
<td>2,994</td>
<td>22.0%</td>
<td>3,789</td>
<td>26.6%</td>
<td>6,285</td>
<td>65.9%</td>
<td>7,482</td>
<td>19.1%</td>
</tr>
<tr>
<td>Brazil</td>
<td>1,137</td>
<td>-8.8%</td>
<td>1,785</td>
<td>56.9%</td>
<td>2,411</td>
<td>35.1%</td>
<td>3,063</td>
<td>27.1%</td>
<td>3,487</td>
<td>13.8%</td>
</tr>
<tr>
<td>Chile</td>
<td>517</td>
<td>13.9%</td>
<td>708</td>
<td>36.9%</td>
<td>1,151</td>
<td>62.5%</td>
<td>1,566</td>
<td>36.1%</td>
<td>3,115</td>
<td>98.9%</td>
</tr>
<tr>
<td>Argentina</td>
<td>161</td>
<td>214%</td>
<td>239</td>
<td>48.1%</td>
<td>309</td>
<td>29.2%</td>
<td>331</td>
<td>7.1%</td>
<td>489</td>
<td>47.8%</td>
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</tbody>
</table>

Source: Data from Korea International Trade Association (KITA)
<Table 2> Current situation of the imports by Korea's key regions

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<tr>
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<th></th>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Mexico</td>
<td>334</td>
<td>13.0%</td>
<td>411</td>
<td>23.2%</td>
<td>460</td>
<td>11.8%</td>
<td>798</td>
<td>73.5%</td>
<td>1,013</td>
<td>26.9%</td>
</tr>
<tr>
<td>Brazil</td>
<td>1,619</td>
<td>29.7%</td>
<td>2,195</td>
<td>35.6%</td>
<td>2,501</td>
<td>13.9%</td>
<td>2,707</td>
<td>8.2%</td>
<td>2,794</td>
<td>3.2%</td>
</tr>
<tr>
<td>Chile</td>
<td>1,058</td>
<td>40.3%</td>
<td>1,934</td>
<td>82.8%</td>
<td>2,279</td>
<td>17.9%</td>
<td>3,813</td>
<td>67.3%</td>
<td>4,184</td>
<td>9.7%</td>
</tr>
<tr>
<td>Argentina</td>
<td>436</td>
<td>15.7%</td>
<td>421</td>
<td>-3.3%</td>
<td>372</td>
<td>-12%</td>
<td>556</td>
<td>49.6%</td>
<td>732</td>
<td>31.6%</td>
</tr>
</tbody>
</table>

Income from the trade with Mexico grew 26.9% in 2007 compared to the previous year, and export too is growing steadily. Korea’s imports from Brazil are growing quickly due to the growing demand for raw materials. In the case of Chile, a growth rate of 9.7% was recorded in 2007 which by comparison was a significant decline to the previous year.

2. Current situation on trade by product category

Upon examination of products exported to Latin America from Korea, electronic parts take up a significant portion, especially in relationship to Mexico, which stems from the demand of the Korean companies entering into local markets. Brazil’s share of the electronic export goods is rather high. In the case of electronic industrial goods, sales decreased somewhat in 2007. However, they are still the highest share logged in terms of amount. Conveyor machinery is growing steadily buoyed by the demand in local markets. In Chile, exports of petroleum products increased 266.5% in 2007 as compared to the previous year.

<Table 3> Current situation of Korea’s exports by key product categories

<table>
<thead>
<tr>
<th>Country</th>
<th>2004</th>
<th>2005</th>
<th>2006</th>
<th>2007</th>
</tr>
</thead>
<tbody>
<tr>
<td>Mexico</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>LCD device</td>
<td>34(104.7%)</td>
<td>133(289.2%)</td>
<td>1,097(723.0%)</td>
<td>2,387(117.7%)</td>
</tr>
<tr>
<td>Color TV parts</td>
<td>487(255.6%)</td>
<td>959(96.8%)</td>
<td>1,509(57.4%)</td>
<td>1,497(-0.8%)</td>
</tr>
<tr>
<td>Automobile parts</td>
<td>40(9.3%)</td>
<td>58(43.7%)</td>
<td>100(72.2%)</td>
<td>284(184.6%)</td>
</tr>
<tr>
<td>Brazil</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Industrial</td>
<td>873(78.3%)</td>
<td>1,167(33.6%)</td>
<td>1,304(11.7%)</td>
<td>1,136(-12.9%)</td>
</tr>
<tr>
<td>electronic goods</td>
<td></td>
<td></td>
<td></td>
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</tr>
</tbody>
</table>
Likewise, exports of petroleum products are faring well, but they are in the red when compared to the total imports. Argentinean exports of polyester products declined somewhat in 2006. However, since 2007 they have started to grow once again. In the case of the vehicle growth rates; freight vehicle exports are particularly noticeable.

*Table 4* Current situation of the imports by key products

(Unit: Million USD, %)

| Source: KITA |
|-----------------|-------------------|-----------------|-------------------|-----------------|
| **Conveyor machinery** | **Electronic goods parts** | **Petroleum products** | **Vehicles** | **Wireless communication device** |
| **Mexico** | **Zinc ore** | **Slab** | **Argentina** | **Polyester resin** | **Freight vehicles** | **CRT TV** |
| **Unrefined copper ingot** | **(616.8%)** | **31.7%** | **133(160.2%)** | **285(244.6%)** | **589(106.5%)** | **221(87.8%)** | **285(29.0%)** | **368(29.0%)** | **457(24.3%)** | **67(-18.5%)** | **241(262.3%)** | **494(104.7%)** | **1,811(266.5%)** | **251(54.4%)** | **370(47.7%)** | **482(30.2%)** | **672(39.5%)** | **60(142.1%)** | **100(66.6%)** | **99(-0.7%)** | **95(-4.6%)** | **20(-23.0%)** | **46(130.7%)** | **36(-23.1%)** | **59(66.6%)** | **1(83.9%)** | **5(270.7%)** | **11(101.6%)** | **18(75.3%)** | **2(24.2%)** | **60(33.1%)** | **498(-17.1%)** | **522(4.7%)** | **954(86.0%)** | **871(-8.7%)** | **1,621(108.3%)** | **1,866(266.5%)** | **513(142.2%)** | **657(84.0%)** | **1,369(108.3%)** | **1,274(39.5%)** | **95(10.0%)** | **108(14.3%)** | **129(19.4%)** | **227(75.7%)** | **95(6.2%)** | **26(-74.0%)** | **188(663.6%)** | **281(49.7%)** | **140(137.8%)** | **114(-18.2%)** | **120(4.5%)** | **143(19.5%)** | **8(523.8%)** | **10(28.5%)** | **23(133.5%)** | **37(63.2%)** |
Meanwhile, minerals are the key import product into Korea from Latin America. In Mexico, imported unrefined copper ingot takes up the highest share. Brazil is also a key raw ingredient supply nation for Korea, and exports high quantities of minerals and agricultural products. The Chilean economy is very dependent on copper according to several measures. Over 70% of the trade with Chile is limited to the raw material copper which places a financial strain on trade relations between Korea and Chile. Trade with Argentina is also heavily focused on the import of raw materials and although imports decreased somewhat in 2005, since 2006 they have been increasing.

III. Key Trade Regulation Policy in the Latin American Regions

Until the late 1980s, Latin America made headlines as a place associated with revolutions and coups. Latin American nations have implemented all types of trade liberalization policies while at the same time forming integrated economy bloc for each region. They are seeking ways to increase trade within the region and pursuing after stable economy growth. However, such regional economic integration and trade barriers, such as tariffs, make it difficult for the Korean companies to export to local markets.

1. Import Regulation Measures

The basic principle of the international trade environment, centered on the GATT/WTO system, is to realize the liberalization and fairness of international transactions. In other words, tariffs and non-tariffs obstacles are to be mitigated or eliminated altogether and all types of regulations are to be corrected, to realize fair trade. In general, import regulation refers to the measures that affect imports such as approvals for import and import quota. In particular, import quota is likely to restrict free trade when compared to tariffs. Thus, Sub Clause 4

9) Import Licensing is defined as administrative procedures used for the operation of import licensing regimes requiring the submission of an application or other documentation(other than required for customs purposes) to the relevant administrative body as a prior condition for importation into the customs territory of the importing member. WTO Annex 1A, Agreement on Import Licensing Procedures.
10) No prohibitions or restrictions other than duties, taxes or other charges, whether made effective through quotas, import or export licenses, shall be instituted or maintained by any contracting party on the importation of any product of the territory of any other contracting party or on the exportation or sale for export of any product destined for the territory of any other
of Clause 11 of the GATT also strictly regulates against limiting quantity. In Mexico which implemented liberalization policies in a full-fledged manner after the launch of NAFTA, there are few product categories that are banned from importation with the exception of certain few particular categories in congruence with other nations. In accordance with this, economic government authority (Secretaria de Economia)'s approval (padron de importacion) is required for some categories. In the case of Brazil, it limits the quantity as a measure to restrict import. In particular, a strict measure against Asian woven fabrics has been affected. In 2002, it implemented measures to limit the quantity of Korean woven fabrics. In Chile, there are no particular import regulation measures occurring after the signing of the FTA with Korea. However, imports of used vehicles are prohibited and foodstuff and medications require approval of related institutions. Argentina has temporary one-time restrictions on the quantity imports when it comes to some product categories such as vehicles. Medications require approval in advance. In fact, at least three years are required to obtain approval of Korean medications. As for the categories that are prohibited for importation, they include used vehicles and used medical devices.

2. Customs and tariffs measures

Mexico, based on the 1990 “Decreto para el fomento y modernizacion de la industria automotoriz” allows only those companies that assemble and produce in Mexico to import finished vehicles. However, this law was abolished in 2004 during the UR negotiations. Mexico levies high tariffs for imports when it comes to the nations that did not sign the FTA with Mexico. Thus, exporting vehicles to Mexico is indeed difficult. Mexico levies a 10% tariff on at least 50% of all the imports. In the case of vehicles, it levies 50% tariff. In particular, it is mandatory when custom clears imported products that the standard price for each category should be officially posted up. When imported at a lower price, price certificates needs to be attached so that importation at low price can be regulated. Meanwhile, according to a WTO announcement, Mexico is a nation that frequently investigates dumping practices. Filing a suit against dumping practices can be placed by the companies or organizations that produce at least 25% of the domestic production, and a decision to either to investigate or not should be made within 30 days after the application is received. Preliminary judgment should be conducted within 130 days after the start of the investigation, and final judgment is required within 260 days.

12) Refer to the following site to refer to the list of related institutions that issue approval for the categories that can be imported. http://www.aduana.cl/prontus-aduana/site/artic/20070228/pags/20070228161116.html
13) Due to the abolishment of this law, Mexico does not restrict the importation of new vehicles from USA, Canada, and EU.
14) ILSEN, La industria automotoriz en el Tratado de Libre Comercio de America del Norte: Implicaciones para Mexico, 2003, pp.48-49.
Brazil, a member nation of the MERCOSUR, applies a 0-35% Common External Tariff (CET) for imports from nations other than the MERCOSUR, depending on the products. Moreover, it is customary to pay tax by leveraging with a customs agent due to complex customs procedures. There are also many instances in which importation is restricted by stepping up the customs inspection. In Chile, it levies up to 24% anti dumping and countervailing duties if it sees the possibility that the domestic industry may be hurt by the dumping or subsidy of the exporting nation. An extension every one year is possible. In the case of Argentina, another MERCOSUR member nation, it applies Common External Tariff, but levies tariff of 35% for the vehicles. For electronic goods, which are Korea's key exports, 20% Common External Tariff is levied. In particular, significant lead time to clear the customs is required due to the introduction of the Canal Morado method when clearing customs imports.

Moreover, a minimum import price system is enforced to defend against instances in which the price of imports is lower than the minimum price defined by the government. Some Korean products including clothing and parts are included in this. In addition, Argentina is one of the representative nations that enforce anti-dumping measures. Starting from 1995 to 2001, it took on a total of 96 cases of anti-dumping measures. Even today, Argentina regulates imports by investigating anti dumping at all times to protect its domestic industry.

IV. Korea's Countermeasures

1. Pursuit of FTA with the key Latin American nations

Starting in the 1990's, Latin American nations became aware of the world economy's trend to form economic blocs and of the need to actively pursue economic integration in their regions. The nations have actively used protectionism policies to support other goals. Presently, economy integration of the Latin American regions takes

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15) MERCOSUR, launched officially on 1st January 1995, is a trade bloc, but it also is geared towards forming a single market. It attempts to cast away the economic binding of the advanced nations as well as pursuing after the economic gain of the nations in the bloc. MERCOSUR is made up of Brazil, Argentina, Paraguay and Uruguay together with Chile. see Tayana(2004) and Blum(2000).


18) In the past, “Canal Verde” referred to immediate customs clearance while “Canal Naranja” required one to two days after reviewing documents. “Canal Roja” required three to four days for reviewing documents and inspecting goods.


20) Most Latin American nations grew less than 30% in per capita terms between 1985 and 1998, see Contreras(2001).

place with the FTA because it enables them to set tariffs on their own. Moreover, given the economic situation and political factors among the Latin American nations, there are some obstacles that impede them from moving up to the Customs Union stage. However, the MERCOSUR is not a FTA, but a Customs Union. Thus, it levies Common External Tariff on those nations that are not in the bloc. Currently, each of the Latin American nations signs a regional trade agreement despite their geographic location if the agreement is helpful for their domestic economy. Korea-Chile FTA is a representative example. In particular, Chile signed with most of the Latin American nations giving it the potential to serve as a stronghold for the Korea's increased export and investment in Latin America. In addition, the negotiation know-how accumulated while pursuing the FTA with Chile can be leveraged as a strategy when negotiating with other Latin American nations.

Presently, Korea is working to sign the FTA with Mexico. After agreeing to a joint study with Mexico in 2004 for the pursuit of the FTA, Korea is pursuing FTA negotiation in a full-fledged manner starting from 2007. If the Korea-Chile FTA is to serve as the bridge that will enable South Korea to preempt the South America region, signing of the FTA with Mexico will serve to enter into the Central America region.

Furthermore, Korea started a joint study with MERCOSUR, the largest integrated economy bloc in the Latin American regions in 2004 to examine the possibility of signing FTA with the MERCOSUR. MERCOSUR takes up 71% of the land mass in Latin America, and it is a very important market that amounts to 100 Million USD. In particular, the reason that Korea needs to actively walk into the FTA negotiation with the Latin American regions is that it needs to prepare against the FTAA as well as seek to eliminate import obstacles. If FTAA is to be launched officially, then Korea cannot help but compete with Latin American nations in North America. Thus, Korea needs to actively pursue FTA with the Latin American nations. At the same time, it needs to explore a strategy that will prepare against the launch of the FTAA.

2. Increased investment in the local markets and the strategy to diversify exports

Currently, Mexico’s primary demand for the Korea-Mexico FTA is Korea’s increased investment. In fact, Korea’s investment in Mexico in the Latin American regions is significantly high. Despite it all, however, Mexico is demanding

22) Chile's bid to become a full member of NAFTA and of MERCOSUR, see Sznajder(1996).
23) see Moreno, pp.411-418.
24) FTAA is the negotiation that the USA is focused on the most in terms of the external trade policy. In 1990, the USA proposed the Enterprise for the Americas Initiative (EAI) with the goal of 34 nations in the Americas signing this agreement until 2005, see Smith(2000). However, this initiative is currently stalled. However, if FTAA is to be launched officially, it is expected to become the world's largest free trade zone and significantly influence nonmember nations including Korea.
that Korea increase investments in Mexico, citing other nations' investments. Except for the oil drilling and other areas that are not available for foreign investment, according to the Mexico's Foreign Investment Law, almost all other business areas are available for foreign investment.

Latin American regions lack development capability even when they enjoy rich oil and mineral reserves. Thus, it is necessary to participate actively in the development of resources. In the case of Brazil, a 200,000.00 USD deposit in the Banco Central is required for a foreign company to establish a corporation in Brazil. In this case, if a foreign invested company chooses to establish a corporation to participate in local mining business, they are subject to equal treatment as if they were a local company and can hold upwards of 50% of the shares. Because Brazil has many natural resources, there are many opportunities to participate in the resource development initiatives. The mineral resources currently known are presumed to be merely 10% of the total natural resources available. Currently, key multinational companies in the world are actively announcing their plan to participate in the development projects. Korea too needs to participate actively, especially since it also imports these natural resources.

Korea's only direct investment for the resources development business in Brazil is conducted through the KOBRASCO, which is a JV company, formed with the CVRD26), a steel company in Brazil. The reasons that the investment in the resources development in Brazil is low are due to lack of information and concern for the local economy.27)

In the case of Chile, Clause 10.328) of the agreement between Korea and Chile applies the principle of National Treatment29), with no special treatment granted to foreign investors. Chile is often the first stop for investors entering Latin America. Investment is relatively free in Argentina. However, Argentina is sued by many foreign investors, for violating investment agreements. In terms of the amount, a total of 15.5 Billion USD investments were made30) because Argentina attracted a significant amount of foreign capital during the privatization of public companies. However, the existing policy gave special treatment for foreign investors that collapsed due to the economic crisis during the early 2000s. Argentina's policy to attract investment may change depending on its economic situation. Thus, JV investment with a local company is recommended instead of investing alone.

Until now, Latin American markets were considered the markets to dispose of bad inventory. Only limited product

26) CVRD, a steel and mineral producer, established in 1942 grew into Brazil's largest company, buoyed by China's increased import of the raw materials and price increase in the world. It exerts significant influence in the steel and mineral price in the world.
28) Each Party shall accord to investors of the other Party treatment no less favourable than that it accords, in like circumstances, to its own investors with respect to the establishment, acquisition, expansion, management, conduct, operation, and sale or other disposition of investments.
29) The second major obligation of nondiscriminatory treatment, after MFN, is the national treatment obligation, see Jackson (1997).
assortment was exported. However, it is now time to develop new strategies. In particular, Latin American regions are becoming hot IT markets. According to the report of the World Economic Forum (WEF), currently Korea has the 9th IT competitiveness in the world after the Iceland. Accordingly, Korea needs to diversify its exports, leveraging its world-class semiconductors, wireless communication devices and so forth to penetrate the market.

V. Conclusion

Currently, Latin American economy is experiencing continual growth and is consolidating its position as an important player in the global market. Moreover, it is trying to generate economy of scale and to increase trade through economy integration. Although it can be said that Korea secured the opportunity to enter into the Latin American markets by signing the FTA with Chile, there are many issues to resolve. In particular, Latin American regions are taking measures to restrict imports such as limiting the quantity and by implementing differentiated tariffs for the nations that are not included in the bloc. Thus, this research proposes two measures when it comes to increased participation in the Latin American markets. The first measure is the signing of the FTA with key Latin American nations. It is necessary to sign FTA with Mexico to penetrate Central America, distinguishing it from other Latin America regions. In South America, it is necessary to pursue the strategy of expanding the market centered on the MERCOSUR. In particular, given the likelihood of launching the FTAA later on, and given the integrated economy bloc of Latin American regions, it is necessary to actively pursue FTA with other key nations. The second measure states it is essential to increase local investment and diversify products for trade. Although Latin American regions hold rich natural resources, they lack the development ability. Thus, they are actively seeking foreign investment. Given that the Latin American nations are key exporters of the raw materials that are in demand in Korea, it is necessary to approach local resource development efforts in a strategic manner. Moreover, Latin American markets should not be perceived as the places to discard bad inventory, but to consider them markets for exporting technology intensive places to diversify products.
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